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¶1. (SBU) Summary: Australia's extensive and growing Liquefied Natural Gas (LNG) industry is up in arms about the Government's plan to create an emissions trading scheme (ETS) because the Government's discussion paper (aka green paper) on emissions trading (reftel A) failed to indicate whether LNG is an emissions intensive trade exposed (EITE) industry. The paper set a lower threshold of 1500 tons of CO_2 equivalent emitted per million dollars (A$) of revenue to determine who will get free permits to protect against trade exposure. Because large LNG players claim they will fall below this cut-off, LNG companies have expressed concerns about losing LNG projects in Australia. The Australian government has indicated that it recognizes this may be an issue to resolve, and further talks between GOA and the LNG industry will try to set out exactly where LNG should fall under the scheme. End summary.

WHAT IS AT RISK?

¶2. (SBU) The Australian LNG industry is concerned because the GOA green paper does not initially address LNG as an industry that should receive some protection against being exposed under a carbon scheme to a world price and lower competitiveness. They argue that billions of dollars worth of planned investments are in danger because being forced to pay for carbon emissions would make Australia less competitive as an investment destination. The green paper acknowledges that "significant further analysis" is required to address industries that request EITE assistance. The LNG industry has estimated that nearly A$60 billion of investment could be deferred or sent elsewhere if Australia's emissions trading system does not protect LNG as a trade exposed, emissions-intensive industry with access to free permits.

LNG INDUSTRY REACTION TO GREEN PAPER

¶3. (SBU) On July 29 Econoff spoke with Damien Dwyer of the Australian Petroleum Production and Exploration Association (APPEA) about the LNG sector's reaction to the green paper. According to Dwyer, major LNG players feel the potential loss of A$60 billion in investment is a concern for the whole industry. Dwyer pointed out that the boom-bust LNG cycle in Australia is driven by world prices, unaffected by domestic

measures that distort pricing like the ETS, and therefore investment may flee to countries with less stringent emissions policies. Although LNG might be profitable now, Dwyer said, there is a concern that the use of revenue as a denominator discriminates against the booming LNG sector and will fail to provide the protection needed to maintain expansion plans in Australia when costs rise and revenues fall. Dwyer said APPEA is working to ensure that LNG will be recognized as a trade exposed industry regardless of the actual emissions intensity of the companies and processes involved. The best possible outcome, Dwyer believes, is no net increase in operating costs for LNG under an emissions trading scheme. Despite the relatively positive spin in the press that LNG will be accommodated in some way, Dwyer said is uncertain whether the government's decision will mirror industry's desired outcome.

¶4. (SBU) APPEA's goal of eliminating net increases in
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operating costs under the ETS may be stymied by the government's willingness to challenge the hugely profitable sector. Department of Climate Change Assistant Secretary Barry Sterland told Econoff on August 5 that the paper had achieved its aim of "making clear that there will be costs associated with this." Sterland said the government was concerned about "pork-barreling" in setting up the scheme and that the White Paper on the system's design will likely try and prevent special consideration of any sector or process. How that plays with the range of industries, including LNG, that face higher costs under the scheme remains to be seen.

¶5. (SBU) John Torkington from the Chevron Corporation told Econoff on July 30 that the green paper's recommendations if implemented "would effectively double the operating cost of LNG projects." Torkington refrained from commenting further

because "without trajectories and anticipated emissions prices, it is very hard to be more specific about how this might impact the industry in the longer term." Those trajectories and costs should become clearer when the government releases in October data from modeling undertaken by Treasury. According to Torkington, Chevron supports an ETS within Australia, but he feels that the country should understand "international competitors do not face similar costs on their emissions." On August 11 Torkington told Econoff that if the government's goal was to provide some form of business certainty, they had erred in using the most volatile measure, revenue, as a deciding factor in whether a process would be assessed as trade-exposed. This, combined with the fact that the GOA has decided to close off any possibility of being added to the EITE list after the scheme goes into effect, has driven suspicions that Canberra believes the big players will not walk away from the huge gas finds (Gorgon is believed to hold one quarter of all the gas found off Australia to date) and will grudgingly accept the costs of the ETS in order to stay in the market.

¶6. (SBU) The Rudd Government, and the Carpenter state government in WA, may be right. Torkington told us that even though Chevron has other options for investment, the fear that the GOA might void their tenancy rights over gas they paid hundreds of millions to find is a powerful incentive to remain. The fear that competitors might gain access to gas fields like Gorgon or Wheatstone if left undeveloped because of ETS costs may well in the end drive LNG players to grit their teeth and go along after getting whatever level of special compensation they can wring from Canberra.

¶7. (SBU) BP's Ian Singleton, Manager for the large Browse project, said BP was concerned about emissions trading costs, but was also concerned about Browse partners like Woodside's Don Voelte pressing ahead so aggressively. Singleton said that the big players were in position to pay ETS costs as long as profits were high, and that "we have to be where the gas is". BP is equally concerned with their refinery sector

in Australia, which they see as more at risk of being off-shored rapidly (reftel B).

GOVERNMENT SHIFT?

¶8. (SBU) Two major events have dominated the public debate concerning government and LNG industry relations: Opposition Shadow Treasurer Malcolm Turnbull's visit to LNG facilities in Western Australia, and Prime Minister Rudd's direct response saying he was open to further consideration on the question of protecting the LNG industry during his July visit to the Northern Territory. Dwyer suggested that the media reports may have gone "a little too far" as government-industry consulting still must take place. Given the size and importance of LNG as an export product for Australia, it is likely that the GOA is considering some flexibility in how they accommodate the industry. To spur that on, sources tell us that the major industry players, including Exxon Mobil, Chevron, BP, and Woodside are writing to Rudd to argue against a number of elements in the scheme, including EITE status. That this letter is going to Rudd, rather than Climate Minister Wong, indicates how seriously Qrather than Climate Minister Wong, indicates how seriously the companies involved take this issue.

¶9. (SBU) Comment: Even if big players are carping loudly while preparing to go along in 2010, their complaints have had some effect. Sterland refused to be drawn out on possible changes to the plan during a meeting with Econoff on August 5, but the Western Australia Government's Emissions Trading manager Amy Lomas told us that she has heard that DCC is reconsidering the formula for determining EITE status and may move away from the revenue calculation. Western Australia is frustrated that Canberra has not listened to their concerns about possible impacts of the ETS on core industries in the state. This view was backed up by WA Department of Premier and Cabinet Environment Direct Rosh Ireland. The challenge of being heard has not been helped by the decision to call a snap election in the state, which has placed the government in caretaker mode. This has delayed the approval of draft submissions to Canberra on the ETS until after the elections in September. End Comment.

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